

recovery and phasing out the remainder of the RIC through market-based or regulatory processes -- was favored by a number of commenting parties, including TCG.<sup>30</sup> A number of parties pointed out that the Commission is required, under the Telecommunications Act of 1996, to eliminate implicit subsidy arrangements, and for that reason as well must eliminate the RIC.

In its initial Comments, TCG suggested that any amounts remaining in the RIC should be recovered through a uniform surcharge on all local transport elements, since the costs in the RIC are related to local transport. Since that portion of the switched access market is subject to more competition than the local loop or local switch, pushing the recovery of the remaining RIC amounts to transport will provide the most effective means for the industry to "compete away" these amounts.

Several parties suggest that the Commission ensure that parties that use CLEC switched access transport facilities not be charged by the ILEC for any RIC elements.<sup>31</sup> TCG's proposal, which would collect the RIC through a surcharge on ILEC transport services, would achieve the same goal, and would ensure that

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<sup>30</sup>See, e.g., TCG Comments at 29-33; USTA at 58-59; Frontier Comments at 9; ALTS Comments at 26; TCI Comments at 20.

<sup>31</sup>Time Warner Communications at 12-15 ["If the commission decides to retain the [RIC] for a period of time ... such a charge should not be imposed where a CAP provides transport services. In no case should CAPs be required to pay for the costs of their competitors in the access market."]; WorldCom at 64.

users of alternative transport facilities not be required to pay for the costs of the ILEC's transport network through the imposition of RIC charges.

If, however, the Commission were to continue to allow the remaining RIC amounts to be collected by the ILEC from end office based charges, then the suggestions of these parties should be given serious consideration. Adopting such a policy would, in fact, be consistent with the views of the Colorado Public Utilities Commission. That Commission ordered that US West not collect any RIC charges from carriers who utilize alternative transport facilities, and that if both US West and a CLEC jointly provide the transport services, the RIC should be shared.

The Colorado Commission said:

[s]pecifically as to the RIC ... [i]f USWC is not providing the transport of a call from an end-office switch to an IXC, then USWC may not apply its switched access transport rates, including the RIC, to those calls.<sup>32</sup>

In its reconsideration order, the Colorado Commission reiterated its views, as follows:

If US West does not provide any of the transport, it shall not, as stated in the Order, apply its RIC to such calls. We clarify our Order as to the application of the RIC. The RIC shall be applied on a pro rata basis determined from the proportional distance between the TCG tandem and the end-office of USWC. In this instance, if USWC supplies all of the transport for the call, it would apply 100 percent of the RIC. If a mid-span meet-point is used, only one-half of the RIC would be applicable. ... We also note that this issue of the reasonableness of the RIC and its continued existence has been remanded by the United States Court of Appeals back to the FCC for

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<sup>32</sup>TCG Colorado Petition for Arbitration, Decision No. C96-1186, November 8, 1996, at 41.

reconsideration and will be revisited by the FCC in the near future. Our decision provides a means of properly compensating either party for its costs regardless of the existence of the RIC.<sup>33</sup>

As the Colorado Commission recognized, there is a fundamental unfairness in allowing an ILEC to collect local transport related RIC charges from IXC's that are using CLEC facilities. The Commission must ensure, to the extent that any RIC type charges remain, that they be collected in a manner that does not force users of competing transport services to subsidize the ILEC's transport services. Such a result -- which applies today -- serves to create a true "competitive disadvantage" for new entrants like TCG.

**IV. NUMEROUS COMMENTERS AGREE THAT THE COMMISSION'S PROPOSED MARKET-BASED APPROACH WILL HINDER THE DEVELOPMENT OF EFFECTIVE COMPETITION.**

**A. THE COMMISSION'S MARKET-BASED PROPOSAL INAPPROPRIATELY SETS A VERY LOW THRESHOLD FOR SIGNIFICANT AND SUBSTANTIAL DEREGULATION.**

In the Notice, the Commission recommended reducing price-cap ILEC regulation in two phases as competitive benchmarks are achieved. Phase I of the Commission's proposed plan provides that once an ILEC has demonstrated that "Potential Competition" has been met for a particular service, the Commission would permit geographic deaveraging within a study area, volume and term

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<sup>33</sup>TCG Colorado Petition for Arbitration, Decision No. C96-1344, December 27, 1996, at 5-6.

discounts for access services, easier ability to offer new, innovative access services, as well as contract tariffs and individual request for proposals (RFPs). The proposed threshold for demonstrating "potential competition" is very low, essentially mirroring the unbundling and equal access requirements set forth in the 1996 Act, which ILECs are required to satisfy anyway.<sup>34</sup>

Virtually none of the 105 parties participating in this proceeding support the Commission's market-based approach to deregulation as proposed in the Notice. Indeed, a significant number of the commenters agree that the Commission's requirements for meeting the Phase I test are too low or are otherwise unworkable.<sup>35</sup> The basic flaw with the proposed market-based approach is that the Phase I standards impose no new conditions on ILECs as a requirement for receiving such significant deregulation. As NCTA states "... the Phase I criteria constitute obligations to which BOCs in particular are already subject. In this

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<sup>34</sup>Notice at ¶163.

<sup>35</sup>See, generally, Comments of Alabama Public Service Commission, Association for Local Telecommunications Services (ALTS), AT&T Corporation (AT&T), Cable and Wireless, Inc. (CWI), Competition Policy Institute (CPI), Competitive Telecommunications Association (CompTel), ICG Telecom Group, Inc. (ICG), District of Columbia Public Service Commission, (DC PSC), Florida Public Service Commission (FPSC), MCI Telecommunications Corporation (MCI), Missouri Public Service Commission, National Cable Television Association (NCTA), Sprint Corporation (Sprint), Tele-Communications Inc. (TCI), Telecommunications Resellers Association (TRA), Texas Office of Public Utility Counsel (Texas PUC), Time Warner Communications Holdings, Inc. (Time Warner), and Worldcom, Inc. (Worldcom).

sense, Phase I can be interpreted as a proposal to grant ILECs pricing flexibility merely because the Telecommunications Act has become law."<sup>36</sup> Although the Phase I standard appears to offer the added requirement of "rapid provisioning of network elements", at least one RBOC -- Ameritech -- already taken the position that the mere "offering" of access to unbundled network elements constitutes "provisioning" of network elements.<sup>37</sup> The "rapid provisioning" requirement must certainly be given more "teeth" than Ameritech's application would have it, but even that requirement does not address the quality, pricing, or other characteristics of interconnection.<sup>38</sup>

The Commission's low threshold for potential competition arguably will allow substantial deregulation while placing no additional burdens on the ILECs to

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<sup>36</sup>NCTA Comments at 9. See also ICG Telecom Group Inc. At 10. ICG pointed out that the Notice's proposals fall short of meeting the standard set by the Act and the Commission's own standards for relaxed regulation. ICG argued that it would be incongruous and arbitrary for the Commission to pronounce relaxed regulation for ILECs before all the statutory criteria are met and before the issues and rates in Expanded Interconnection have been addressed. ICG at 10.

<sup>37</sup>See Application by Ameritech Michigan Pursuant to Section 271 of the Telecommunications act of 1996 to Provide In-Region, InterLATA Services in Michigan, CC Docket No. 97-1, filed January 2, 1997, withdrawn February 13, 1997. Ameritech claimed that its interconnection agreements with competitive carriers would satisfy any provisioning requirements.

<sup>38</sup>Even where TCG has concluded arbitrations the costs underlying the interim rates generally are still not based on forward looking cost studies; in fact, no state has yet completed a review of properly performed cost studies. Thus, TCG's arbitrated agreement in Michigan only provides for interim rates for interconnection and unbundled network elements.

demonstrate that competition exists. As Sprint stated in its comments, "[a]ll that the satisfaction of the Phase One triggers guarantees is that legal and regulatory barriers to competitive local entry have been removed, not that new entry is economically feasible or that it will actually occur."<sup>39</sup>

Moreover, as TCG stated in its comments, the relief that an ILEC would obtain once it has met the potential competition threshold would virtually deregulate the ILECs' access offerings, particularly with regard to contract tariffs and RFPs. Contrary to the Commission's goal of explicitly associating Switched Access charges with their underlying costs, there is a serious risk that contract tariffs and RFPs may not be cost based. The Commission's requirements of cost justification under ICBs may provide no meaningful opportunity to ensure that rates are fair, non-discriminatory, and not predatory in effect.

In support of this position, MCI noted that the Commission's proposal to grant contract tariff authority to incumbent LECs who have met the "potential competition" checklist is contrary to Commission precedent.<sup>40</sup> MCI pointed out that in an order rejecting Southwestern Bell's attempt to increase its pricing flexibility, the Commission stated: "even in cases where the Commission allowed AT&T to offer some of its long-distance services pursuant to contract carriage

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<sup>39</sup>Sprint Comments at 41.

<sup>40</sup>MCI Comments at 60-61.

rates, the Commission has determined that 'AT&T . . . may include in its contracts only those services the Commission has found to be substantially competitive.' Under the substantial competition test, the potential for strategic pricing is reduced because a competitor has invested substantial sunk costs."<sup>41</sup>

Moreover, the Commission has a long history of applying a market-based approach to deregulation that is gradual and incremental. For example, this approach resulted in the prices of Special Access services dropping substantially, and the quality, variety and timeliness of Special Access services improving dramatically, over the past ten years. These consumer benefits were achieved with little or no regulatory intervention; such intervention was not contemplated until effective competition took hold.<sup>42</sup> It defies logic -- as well as appellate standards for reasoned decision making -- that the Commission would now ignore

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<sup>41</sup>MCI Comments at 60.

<sup>42</sup>TCG's comments listed numerous occasions where this Commission has opted to implement a gradual and incremental approach to deregulation in deregulating AT&T and competitive carriers, and reforming transport rate structure and pricing. See TCG Comments at 33-42. AT&T also addressed the Commission's historical approach toward deregulation stating that "[t]he proposed standards also represent an unexplained departure from past Commission deregulatory policy. AT&T, for example, remained subject to substantial price regulation for over ten years despite its perpetually decreasing market share." AT&T Comments at 76.

its successful past precedent and require merely a "potential competition" standard.<sup>43</sup>

A significant number of commenters expressed similar concerns regarding the Commission's low threshold requirement and the associated substantial deregulation.<sup>44</sup> Sprint, for example, contended that the pricing flexibility that the

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<sup>43</sup>Indeed, the Commission itself recognized that gradual, incremental deregulation of price-cap ILECs is beneficial. As the Commission acknowledged in its Notice, removing regulatory restrictions from interstate access services that are provided by price cap carriers "is consistent with prior decisions in which the FCC *gradually removed* AT&T's services from price cap regulation. Notice at ¶150 (emphasis added) (footnote omitted).

<sup>44</sup>See for example comments of: AT&T Comments at 76; (by prematurely removing the regulatory constraints identified in the NPRM, however, any significant strides toward lower consumer prices, higher quality service, and increased competition will be eviscerated), AT&T at 76; MCI Comments at 45 (premature pricing flexibility would permit the incumbent LEC to reduce access charges selectively in order to deter new entrants); NCTA Comments at 15 (the market-based approach does not calibrate pricing flexibility to the presence of actual competition and reductions of access charges to forward-looking costs); Sprint (although the eventual total deregulation of access, and the removal of access from price regulation, may be laudable goals, such actions should be contemplated only if and when there is sufficiently robust competition, in the form of ubiquitous facilities-based alternatives to the ILECs, to ensure that no carrier can attempt to charge access rates that are above economic costs); TCI Comments at 27 (Commission's proposed market-based approach to access charge reform has two serious flaws: it would rely on the uncertain progress of competition to push access charges down from inefficiently high levels, and it would prematurely allow pricing flexibility that would give ILECs both the ability and incentive to price anticompetitively). See also comments of CPI at 28; ICG at 10; TRA at 7-9; and TWComm at 17-18.



Commission proposed for Phase I would give ILECs unwarranted pricing flexibility in advance of the emergence of any actual competition.<sup>45</sup>

The incumbent LECs asserted that with the availability of unbundled network elements, the Commission can be confident that entry barriers for the competitive provision of access services are low, and, therefore, the Commission's low threshold is justified.<sup>46</sup> They argued that such unbundling guarantees access competition. These competitors, however, did not agree. MCI noted that a purchaser of unbundled elements remains dependent on the incumbent LEC, and further that the ability of new entrants to use unbundled elements remains untested. For these reasons, MCI argued that the Commission should not adopt its tentative conclusion that the ready availability of unbundled elements indicates a high elasticity of supply.<sup>47</sup>

TCG does not oppose deregulation that fosters and supports competition for those services in which competitive options are actually available. However it would be inconsistent with the Commission's traditionally measured approach

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<sup>45</sup>Sprint Comments at 41.

<sup>46</sup>See e.g. Ameritech Comments at 30; Bell Atlantic Telephone Companies (Bell Atlantic) and NYNEX Telephone Companies (NYNEX) Comments at 10; BellSouth Corporation and BellSouth Telecommunications, Inc. (BellSouth) Comments at 27; Pacific Telesis Group (PacTel) Comments at 27; United States Telephone Association (USTA) Comments at 27.

<sup>47</sup>MCI Comments at 67.

toward regulatory changes to deregulate access services in essentially one step, as proposed in Phase I. The radical "flash cut" deregulation proposed in the Notice conflicts with the measured approach to deregulation that was successful as a catalyst to the development of competition. There is no basis for the Commission to depart from its established practice of awaiting the actual development of competition before considering any deregulation of the incumbent monopoly.

While many parties criticized the proposed low threshold, the ILECs -- amazingly enough -- complained that the standards were too high. These ILECs argued that the Commission should provide them with extensive pricing flexibility as soon as one interconnection agreement or a Statement of Generally Available Terms (SGAT) is approved by a state.<sup>48</sup> Since interconnection agreements have been approved, or shortly will be, in most states, the position of these ILECs is that they should be rewarded with substantial deregulations just for "showing up."

USW goes even further to suggest that the Phase I standard should be activated "in a state when an incumbent LEC has in place a signed interconnection agreement for that state without any requirement that the agreement be approved by the state commission."<sup>49</sup>

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<sup>48</sup>See Bell Atlantic/NYNEX Comments at 43; BellSouth Comments at 30; PacTel Comments at 19-20; SWBT Comments at 26; USW Comments at 30; USTA Comments at 27; and SNET Comments at 18-19.

<sup>49</sup>USW at 30. As the Commission recognized in its recent order,  
(continued...)

Merely signing an agreement does not change the natural cross-elasticities of demand in the marketplace. Moreover, an approved interconnection agreement may only provide for resale, in which case Switched Access competition will not be altered. And, of course, an agreement is only paper -- what matters is actual delivery of interconnection services in the market, something the ILEC proposals completely ignore.

For the reasons discussed above, the market-based approach proposed in the Notice and the recommendations made by the incumbent LECs are absolutely untenable. A prematurely deregulated monopoly could endanger the procompetitive objectives of the 1996 Act, and the broader pro-competitive objectives expressed by the Commission itself in its interconnection proceeding and this Notice. TCG and numerous other parties recommend that the Commission avoid "front end loading" extremely substantial deregulatory relief for the incumbent LECs before meaningful local facilities-based competition is observed in the market.

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<sup>49</sup>{...continued)

Ameritech's Section 271 application, an unapproved interconnection agreement is not meaningful. GTE goes even farther than USW by recommending that the pricing flexibility reforms be implemented immediately, eliminating any standard for such relief. GTE at 69.

**B. THE COMMISSION SHOULD FOLLOW ITS SUCCESSFUL METHODOLOGY FOR DEREGULATION AND IMPLEMENT A DISCRETE, STEP-BY-STEP DEREGULATORY STRUCTURE THAT WOULD PERMIT THE COMMISSION TO MEASURE THE AFFECTS OF SWITCHED ACCESS REFORM PRIOR TO IMPLEMENTING DEREGULATION.**

As TCG explained in its Comments, it would be unwise to implement major changes overnight; this would prematurely set up a deregulatory structure prior to determining what are the costs that an ILEC has a legitimate right to recover. The result would be to run the risk of destabilizing both the local and long distance markets. The parties that expressed similar concerns over the market-based approach proposed in the Notice offer a wide array of alternatives. Several parties, for example, advocate that the Commission adopt a prescriptive approach, while some parties recommend an interim prescriptive approach until actual competition develops in the marketplace.<sup>50</sup>

The prescriptive approach, however, is contrary to incentive-based regulation and would place additional administrative burdens on the Commission. For example, CPI's recommendation would require that the Commission annually

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<sup>50</sup>See for example, comments filed by state commissions: Alabama Public Service Commission at 12; California Public Utilities Commission at 17; District of Columbia Public Service Commission at 2; Florida Public Service Commission at 3-5; Missouri Public Service Commission at 5; Texas Office of Public Utility Counsel at 4-5; Texas Public Utility Commission at 23. See also comments filed by CWI, Comptel, MCI, TRA, WorldCom, and TCI. CPI recommends a mixed market and prescriptive approach. CPI at 26.

review the progress of movement of prices toward a predetermined target and decide on an annual basis whether additional prescriptive reductions are necessary. Under CPI's proposed annual review the Commission would need to investigate actual declines in access prices, the extent to which access prices are below price cap ceilings, the quality of unbundled network element provisioning, and market share growth.<sup>51</sup>

The CPI proposal illustrates the basic problem with the prescriptive approach: "[t]he prescriptive approach would launch regulation on a slippery slope of administratively burdensome micro-management."<sup>52</sup> The Commission itself recognized the problematic aspects of a prescriptive approach in its Notice: it requires the Commission to make detailed determinations of appropriate price levels for multiple services throughout the country.<sup>53</sup>

TCG recommended in its Comments that the Commission implement a step-by-step deregulatory structure that will enable the Commission to evaluate the rate structuring plans it will implement as a result of this proceeding. TCG believes that its proposal addresses the concerns that numerous parties raised about the Commission's "front-end" loaded market-based approach. At the same time,

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<sup>51</sup>CPI at 26.

<sup>52</sup>ICC at 15.

<sup>53</sup>Notice at ¶143.

TCG's proposal alleviates the need for the Commission to implement burdensome administrative responsibilities that would result if a prescriptive approach were adopted.

TCG stated that the Commission should begin Phase I by implementing rate structure reforms generally modeled after those described in the Notice, with the modifications described in TCG's Comments and this Reply. These rate structure reforms must be coincident with changes in Universal Service policies. The subsidies currently derived through Switched Access revenues must be reassessed and shifted into the Universal Service funding mechanism.<sup>54</sup> These rate structure reforms are substantial and complex and necessitate ample time to assess whether these specific Commission reforms work successfully. If the Commission were to simultaneously add deregulation policies, it would be unable to accurately assess the result of its reforms.

Moreover, in the absence of Separations reform, there will be little or no change in the total interstate costs assigned to Switched Access, and, therefore, it is not feasible to undertake any substantial changes in overall Switched Access revenues until Separations has been addressed. Despite this fact, the rate structure reforms outlined in the Notice and recommended in TCG's Comments

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<sup>54</sup>Under the Commission's proposal, restructured switching elements may be segregated into flat-rate elements and MOU elements. A similar disaggregation would apply to transport elements.

and these Replies would permit very substantial reductions in the per-minute costs of Switched Access.<sup>55</sup> Thus, even without Separations reform, the Commission's actions can introduce substantial new pricing opportunities for long distance carriers.

The second stage of access charge reform should occur when the Joint Board completes its review of Separations and implements changes affecting the interstate revenue assignments.<sup>56</sup> Implementing a new separations allocation will require adjustments in price levels to conform to any corresponding changes in Separations and lead to lower rate levels. Once in place, Phase I and II will prompt Switched Access prices that more closely reflect their underlying costs.

After Phase I and II fully take effect, the Commission should assess the results of its first two phases of access reform. If the Commission finds that Phase I and II deregulation have been successful, then the Commission can begin to consider market-based deregulation. Phase I will remove the structural problems in the current rate elements. Phase II will more accurately allocate interstate costs. Phase III permits the market to further reduce prices, but only after the market has demonstrated a capability to do so.

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<sup>55</sup>The result would be to permit long distance carriers to offer incremental long distance prices much lower than current access charges permit.

<sup>56</sup>TCG makes this recommendation under the assumption that the Commission's planned Separations reforms will not be completed at the time the Commission is prepared to proceed with its proposed rate structure reform.

**V. CONCLUSION**

For the reasons set forth herein, the Commisison should adopt the recommendations presented by TCG in this proceeding.

Respectfully submitted,

TELEPORT COMMUNICATIONS GROUP INC.

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Dated: February 14, 1997



**REPLY COMMENTS OF TELEPORT COMMUNICATIONS GROUP, INC  
FEBRUARY 14, 1997.**

**ATTACHMENT 1**

# TCG IXC GATEWAY SERVICE<sup>SM</sup>

TCG is now providing Interexchange Carriers an alternative to the switched offering provided by incumbent Local Exchange Companies. Introducing **IXC Gateway Service**...a one-stop entry point for the origination and termination of LATA-wide traffic, utilizing a highly sophisticated network through which all traffic is interconnected, at competitive prices.

## **One-LATA-Wide Connection**

Through just one connection to TCG's superior network, an IXC can handle all LATA-wide originating and terminating traffic, including casual dialed 1+ traffic (10XXX).

Through this one connection, TCG will disperse the IXC's traffic to the appropriate tandem, end office or TCG on-net customers, alleviating the need for the IXC to have multiple trunk groups and facilities to different tandems. **IXC Gateway Service** gives the IXC the opportunity to originate or terminate traffic at ILEC tandems and end offices at rates that are competitively priced.

## **New Business Opportunity**

**IXC Gateway Service** provides the IXC the opportunity to enter intraLATA toll markets without the need to deploy new switching equipment or backhaul to a distant switch. The **IXC Gateway Service** handles all your LATA-wide traffic.

## **State-of-the-Art Network and Switching Technology**

TCG has deployed the latest in **LUCENT** and **NORTEL** generics and switch platforms. Customers will utilize the same state-of-the-art **SONET** technology that has given TCG the edge over other competitors.

In addition, TCG will be one of the first Local Exchange Companies to deploy the **Advanced Intelligent Network** (AIN). This platform allows increased call routing, handling and functionality that provides the IXC with a clear differentiation over services provided by IXCs utilizing other ILECs.

And, TCG has deployed full **Signaling System 7** connectivity throughout its network.

## **Superior Quality and Maintenance**

TCG's **Network Management Center** provides 24 hours a day, 7 days a week network monitoring from two separate locations to keep your communications flowing.

## **Extensive Network Deployment**

TCG provides an extensive network that is interconnected to ILEC tandems and end offices, which allows the IXC to reduce costs and provide a higher grade of service.

## **TEAM TCG**

TCG has put together a unique organization staffed with professionals with years of telecommunications experience. Let **TEAM TCG** show you the most modern telecommunications systems available today.

## **Advantage TCG**

Take advantage of the TCG **IXC Gateway Service**.

- One LATA-wide Connection
- New Business Opportunity
- State-of-the-Art Technology
- Superior Quality and Maintenance
- Extensive Network Deployment
- TEAM TCG
- Competitive Pricing

Your TCG account manager is ready to show you how TCG **IXC Gateway Service** is the IXC's real choice. Call TCG today.



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